

**CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)**

**FINANCIAL STATEMENTS  
AND INDEPENDENT AUDITOR'S REPORT**

**YEAR ENDED JUNE 30, 2006**

## Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

|  |                          |  |                     |
|--|--------------------------|--|---------------------|
| Local Unit of Government Type<br><input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other |                          | Local Unit Name<br>City of Litchfield<br>Tax Increment Finance Authority | County<br>Hillsdale |
| Fiscal Year End<br>6/30/06   | Opinion Date<br>10/05/06 | Date Audit Report Submitted to State<br>11/15/06                         |                     |

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

- |     | YES                                 | NO                       | Check each applicable box below. (See instructions for further detail.)   |
|-----|-------------------------------------|--------------------------|---|
| 1.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.   |
| 2.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.   |
| 3.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.  |
| 4.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit has adopted a budget for all required funds.   |
| 5.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | A public hearing on the budget was held in accordance with State statute.   |
| 6.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.   |
| 7.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.  |
| 8.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit only holds deposits/investments that comply with statutory requirements.   |
| 9.  | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the <i>Bulletin for Audits of Local Units of Government in Michigan</i> , as revised (see Appendix H of Bulletin).  |
| 10. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover. |
| 11. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit is free of repeated comments from previous years.  |
| 12. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The audit opinion is UNQUALIFIED.   |
| 13. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).  |
| 14. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | The board or council approves all invoices prior to payment as required by charter or statute.  |
| 15. | <input checked="" type="checkbox"/> | <input type="checkbox"/> | To our knowledge, bank reconciliations that were reviewed were performed timely.  |

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

|  |                                     |  |             |
|--|-------------------------------------|--|-------------|
| <b>We have enclosed the following:</b>   | Enclosed                            | Not Required (enter a brief justification) |             |
| Financial Statements   | <input checked="" type="checkbox"/> |  |             |
| The letter of Comments and Recommendations                                     | <input type="checkbox"/>            | No audit findings were identified          |             |
| Other (Describe)   | <input type="checkbox"/>            |  |             |
| Certified Public Accountant (Firm Name)<br>Osbourne, March, Condon & Co., P.C. |                                     | Telephone Number<br>517.439.9331           |             |
| Street Address<br>184 W. Carleton Road   |                                     | City<br>Hillsdale                          | State<br>MI |
|  |                                     | Zip<br>49242                               |             |
| Authorizing CPA Signature<br><i>Stephen W. Bisher</i>                          |                                     | Printed Name<br>Stephen W. Bisher          |             |
|  |                                     | License Number<br>1101026492               |             |

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
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Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

184 West Carleton Road

Hillsdale, Michigan 49242

Telephone: 517/439-9331

FAX: 517/439-1894

## INDEPENDENT AUDITOR'S REPORT

To the Tax Increment Financing  
Authority Board  
City of Litchfield, Michigan  
Litchfield, Michigan

We have audited the accompanying financial statements of the governmental activity and major fund activity of the Tax Increment Financing Authority (TIFA), a component unit of City of Litchfield, Michigan, as of June 30, 2006, and for the year then ended. The component unit financial statements are the responsibility of the Tax Increment Financing Authority (TIFA) management, a component unit of City of Litchfield, Michigan. Our responsibility is to express an opinion on these component unit financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the component unit financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the component unit financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the component unit financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activity and major fund activity of the Tax Increment Financing Authority (TIFA), a component unit of City of Litchfield, Michigan, as of June 30, 2006, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages iii through v are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the method of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2006, on our consideration of the Tax Increment Financing Authority's (TIFA), a component unit of City of Litchfield, Michigan, internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be read in conjunction with this report in considering the results of our audit.

*Osbourne, March, Condon & Co P.C.*

Certified Public Accountants

Hillsdale, Michigan  
October 5, 2006

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)

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Management's Discussion and Analysis  
Year Ended June 30, 2006

The following discussion and analysis of the financial performance for the City of Litchfield, Michigan Tax Increment Finance Authority (the "Authority") provides an overview of the Authority's financial activities for the fiscal year ended June 30, 2006. Please read it in conjunction with the Authority's financial statements.

**Financial Highlights**

The following represents the most significant financial highlights for the year ended June 30, 2006:

- The Authority was established in 1984 with an expiration date set at December 31, 2004. Having determined that the goals set forth in the original TIFA development plan have not yet been completed, the City Council approved an extension of the term of existence for a period up to and including December 31, 2025.
- Property taxes are the Authority's single, largest source of revenue. The Authority captured approximately \$36,964,000 of the City's total taxable value for fiscal year ending June 30, 2006, which represents a decrease of \$898,000 or 2.4 percent. Additionally, the Authority captured an average of \$7,291,000 of other local units of government's total taxable value in the City of Litchfield for fiscal year ending June 30, 2006 as well, which represents a decrease of \$5,523,000 or 43.1 percent. These decreases were primarily due to the end of TIFA's capture of school millage after a debt obligation expired.
- Property tax refunds to taxpayers resulting from State Tax Commission and Tribunal adjustments accounted for \$182,573 of the \$200,000 or 120.6 percent increase in other expenses.
- The Authority contributed to the City of Litchfield, Michigan \$10,000 more than it did in the previous year. The additional monies were contributed towards administrative services and capital outlays.
- Development expense increased approximately \$235,000 or 553 percent from the previous year primarily due to housing and industrial park expansion projects. An increase in financial assistance requests from local industrial corporations for expansion of their facilities and enticing prospective new industrial park clients with developmental projects also played a role in the increase.

**Using the Annual Report**

This annual report consists of a series of financial statements. The statement of net assets and the statement of activities provide information about the activities of the Authority as a whole and present a longer-term view of the Authority's finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year and whether the taxpayers have funded the full cost of providing government services.

The fund financial statements present a short-term view; they tell us how the taxpayers' resources were spent during the year, as well as how much is available for future spending. Fund financial statements also report the Authority's operations in more detail than the government-wide financial statements.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)

Management's Discussion and Analysis  
Year Ended June 30, 2006

The Authority as a Whole

The following table shows, in a condensed format, the net assets as of the current in comparison to prior year:

|  | Governmental Activities |                     |
|--|-------------------------|---------------------|
|  | 2006                    | 2005                |
| Assets                                 |                         |                     |
| Current assets                         | \$ 1,952,915            | \$ 2,189,942        |
| Noncurrent assets                      | 1,820,915               | 1,509,746           |
| Total Assets                           | <u>\$ 3,773,830</u>     | <u>\$ 3,699,688</u> |
| Liabilities and Net Assets             |                         |                     |
| Liabilities:                           |                         |                     |
| Current Liabilities                    | \$ 198,756              | \$ 113,004          |
| Net Assets:                            |                         |                     |
| Invested in capital - no related debt  | \$ 299,600              | \$ 305,900          |
| Unrestricted                           | 3,275,474               | 3,280,784           |
| Total Net Assets                       | <u>\$ 3,575,074</u>     | <u>\$ 3,586,684</u> |
| Total Liabilities and Total Net Assets | <u>\$ 3,773,830</u>     | <u>\$ 3,699,688</u> |

The Authority's net assets decreased by approximately .03 percent from a year ago; from \$3.586 million to \$3.575 million.

The decrease in unrestricted net assets of approximately \$5,710 was a planned decrease which was used for development in the City of Litchfield, Michigan industrial park and housing projects.

The following table shows the changes of the net assets during the current year in comparison to prior year:

|                                     | Governmental Activities |                   |
|-------------------------------------|-------------------------|-------------------|
|                                     | 2006                    | 2005              |
| Revenue                             |                         |                   |
| General Revenue:                    |                         |                   |
| Property taxes                      | \$ 564,056              | \$ 719,571        |
| Interest                            | 105,324                 | 36,414            |
| Rental income                       | 33,000                  | 31,625            |
| Total Revenue                       | <u>\$ 702,380</u>       | <u>\$ 787,610</u> |
| Program Expenses                    |                         |                   |
| Development                         | \$ 277,081              | \$ 42,430         |
| Contributions to primary government | 220,300                 | 210,000           |
| Depreciation                        | 6,300                   | 6,300             |
| Other                               | 210,309                 | 16,578            |
| Total Program Expenses              | <u>\$ 713,990</u>       | <u>\$ 275,308</u> |
| Change in Net Assets                | <u>\$ (11,610)</u>      | <u>\$ 512,302</u> |

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)

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Management's Discussion and Analysis  
Year Ended June 30, 2006

**Governmental Activities**

In fiscal year 2006, decreases experienced in property taxes resulted from TIFA no longer capturing school millage. There has been no change in local units operating millage rates that the Authority captures.

As expected, expenses increased to further develop the industrial park and housing for anticipated community growth. In 2006 and 2005 the Authority continued carrying out various development projects through out the City of Litchfield.

**Operating Highlights**

The Authority accounts for all development costs it incurs. The budget in recent years has been developed to continue carrying out a variety of development projects. The budget is developed based on those planned development costs. The budget is monitored closely and amended periodically. The result is that actual revenues and expenses are usually within 10 percent of budgeted amounts.

**Capital Asset and Debt Administration**

At the end of fiscal year 2006, the Authority had approximately \$299,600 (net of depreciation) invested in land and a building that it leases to a local manufacturing business. There is no related infrastructure reported in the year end net capital investment. Any infrastructure developed would be capitalized and depreciated by the City of Litchfield, Michigan.

At June 30, 2006 the Authority did not carry on its financial books any outstanding debt obligations.

**Economic Factors and Next Year's Budgets and Rates**

It is anticipated that property tax revenue collected and reported in the following fiscal year will remain consistent with current year with the exception of a possible increase equal to the rate of inflation.

The Authority will continue the industrial park and housing expansion projects during the upcoming fiscal year.

There were no significant variances between budget and actual results.

**Contacting the City's Management**

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the Authority's finances and to show the Authority's accountability for the money it receives. If you have questions about this report, or need additional information, or would like to obtain financial statements of the City of Litchfield, Michigan, we welcome you to contact the City of Litchfield's administrative office located at 221 Jonesville Street, Litchfield, Michigan 49252.



CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
STATEMENT OF NET ASSETS  
JUNE 30, 2006

|   | <u>GOVERNMENTAL<br/>ACTIVITIES</u> |
|---|------------------------------------|
| ASSETS  |                                    |
| Current Assets:                                 |                                    |
| Cash  | \$ 1,207,755                       |
| Investment                                      | 607,651                            |
| Accounts receivable                             | 277                                |
| Interest receivable                             | 17,678                             |
| Due from other governmental units               | 64,756                             |
| Note receivable, current portion                | <u>54,798</u>                      |
| Total Current Assets                            | <u>\$ 1,952,915</u>                |
| Noncurrent Assets:                              |                                    |
| Note receivable, net of current portion         | \$ 522,183                         |
| Investment in land                              | 189,793                            |
| Infrastructure development                      | 809,339                            |
| Capital assets                                  | 350,000                            |
| Less: accumulated depreciation                  | <u>(50,400)</u>                    |
| Total Noncurrent Assets                         | <u>\$ 1,820,915</u>                |
| TOTAL ASSETS                                    | <u><u>\$ 3,773,830</u></u>         |
| LIABILITIES AND NET ASSETS                      |                                    |
| Current Liabilities:                            |                                    |
| Accounts payable                                | \$ 48,756                          |
| Due to other governmental units                 | <u>150,000</u>                     |
| Total Current Liabilities                       | <u>\$ 198,756</u>                  |
| Net Assets:                                     |                                    |
| Invested in capital assets, net of related debt | \$ 299,600                         |
| Unrestricted                                    | <u>3,275,474</u>                   |
| Total Net Assets                                | <u>\$ 3,575,074</u>                |
| TOTAL LIABILITIES AND NET ASSETS                | <u><u>\$ 3,773,830</u></u>         |

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
STATEMENT OF ACTIVITIES  
YEAR ENDED JUNE 30, 2006

|   | <u>GOVERNMENTAL<br/>ACTIVITIES</u> |
|---|------------------------------------|
| GOVERNMENTAL ACTIVITY EXPENSES          |                                    |
| Development                             | \$ (277,081)                       |
| Contributions to primary government     | (220,300)                          |
| Depreciation                            | (6,300)                            |
| Other                                   | <u>(210,309)</u>                   |
| TOTAL GOVERNMENTAL ACTIVITY EXPENSES    | <u>\$ (713,990)</u>                |
| GENERAL REVENUE                         |                                    |
| Property taxes, captured for operations | \$ 564,056                         |
| Interest                                | 105,324                            |
| Lease income                            | <u>33,000</u>                      |
| TOTAL GENERAL REVENUES                  | <u>\$ 702,380</u>                  |
| CHANGE IN NET ASSETS                    | \$ (11,610)                        |
| NET ASSETS - BEGINNING                  | <u>3,586,684</u>                   |
| NET ASSETS - ENDING                     | <u><u>\$ 3,575,074</u></u>         |

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
BALANCE SHEET - GOVERNMENTAL FUND  
JUNE 30, 2006

|                                    |                     |
|------------------------------------|---------------------|
| ASSETS                             |                     |
| Cash                               | \$ 1,207,755        |
| Investments                        | 607,651             |
| Interest receivable                | 16,845              |
| Due from other governmental units  | <u>64,756</u>       |
|                                    | \$ <u>1,897,007</u> |
| TOTAL ASSETS                       |                     |
| LIABILITIES AND FUND BALANCE       |                     |
| Liabilities:                       |                     |
| Accounts payable                   | \$ 48,756           |
| Due to other governmental units    | <u>150,000</u>      |
| Total Liabilities                  | \$ <u>198,756</u>   |
| Fund Balance:                      |                     |
| Unreserved, undesignated           | \$ <u>1,698,251</u> |
| TOTAL LIABILITIES AND FUND BALANCE | \$ <u>1,897,007</u> |

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
RECONCILIATION OF THE GOVERNMENTAL FUND BALANCE SHEET  
WITH THE STATEMENT OF NET ASSETS  
YEAR ENDED JUNE 30, 2006

|   |    |                         |                |
|---|----|-------------------------|----------------|
| GOVERNMENTAL FUND BALANCE   |    | \$                      | 1,698,251      |
| Amounts reported for governmental activities in the statement of net assets are different because:                                    |    |                         |                |
| Capital assets used in governmental activities are not financial resources, and are not reported in the funds                         |    |                         |                |
| The cost of the capital assets is   | \$ | 350,000                 |                |
| Accumulated depreciation is   |    | <u>(50,400)</u>         |                |
|   |    |                         | 299,600        |
| Notes and accounts receivable are expected to be collected in future years and are not available to pay for current year expenditures |    |                         | 578,091        |
| Investments in land are not a current financial resource and are not reported in the funds  |    |                         | <u>999,132</u> |
| NET ASSETS OF GOVERNMENTAL ACTIVITIES   | \$ | <u><u>3,575,074</u></u> |                |

See accompanying notes to the basic financial statements.

## CITY OF LITCHFIELD, MICHIGAN

## TAX INCREMENT FINANCING AUTHORITY (TIFA)

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN  
FUND BALANCE - BUDGETARY COMPARISON - GOVERNMENTAL FUND

YEAR ENDED JUNE 30, 2006

|                                     | ORIGINAL<br>BUDGET  | FINAL<br>AMENDED<br>BUDGET | ACTUAL              | FINAL TO<br>ACTUAL |
|-------------------------------------|---------------------|----------------------------|---------------------|--------------------|
| REVENUES                            |                     |                            |                     |                    |
| Property taxes                      | \$ 719,569          | \$ 564,515                 | \$ 564,056          | \$ (459)           |
| Interest                            | 40,000              | 64,799                     | 104,491             | 39,692             |
| Lease income                        | 31,625              | 33,000                     | 33,000              |                    |
| Loans collected                     |                     |                            | 25,408              | 25,408             |
| TOTAL REVENUES                      | <u>\$ 791,194</u>   | <u>\$ 662,314</u>          | <u>\$ 726,955</u>   | <u>\$ 64,641</u>   |
| EXPENDITURES                        |                     |                            |                     |                    |
| Development                         | \$ 2,260,000        | \$ 598,802                 | \$ 538,256          | \$ 60,546          |
| Contributions to primary government | 214,000             | 214,000                    | 214,000             |                    |
| Other                               | 43,000              | 217,874                    | 216,886             | 988                |
| TOTAL EXPENDITURES                  | <u>\$ 2,517,000</u> | <u>\$ 1,030,676</u>        | <u>\$ 969,142</u>   | <u>\$ 61,534</u>   |
| NET CHANGE IN FUND BALANCE          | \$ (1,725,806)      | \$ (368,362)               | \$ (242,187)        | \$ 126,175         |
| FUND BALANCE - BEGINNING            | <u>1,940,438</u>    | <u>1,940,438</u>           | <u>1,940,438</u>    |                    |
| FUND BALANCE - ENDING               | <u>\$ 214,632</u>   | <u>\$ 1,572,076</u>        | <u>\$ 1,698,251</u> | <u>\$ 126,175</u>  |

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN

TAX INCREMENT FINANCING AUTHORITY (TIFA)

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES  
IN FUND BALANCES OF GOVERNMENTAL FUND TYPE  
TO THE STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2006

|   |              |
|---|--------------|
| NET CHANGE IN FUND BALANCE - TOTAL GOVERNMENTAL<br>FUND TYPES | \$ (242,187) |
|---|--------------|

Amounts reported for governmental activities in the statement of activities  
are different because:

|   |         |
|---|---------|
| Governmental Funds report capital outlays as expenditures, and in the<br>Statement of Activities these costs are allocated over their estimated<br>useful lives as depreciation | (6,300) |
|---|---------|

|  |          |
|--|----------|
| Collection of long-term receivables is revenue in governmental funds.<br>However, in governmental activities, cash collections reduce<br>long-term receivables | (24,575) |
|--|----------|

|  |                |
|--|----------------|
| Investment in land is an expenditure in governmental funds. However,<br>in governmental activities, the investment is capitalized and<br>recognized as an expenditure when sold. Therefore, the investment<br>is not reported as an expenditure in the statement of activities | <u>261,452</u> |
|--|----------------|

|   |                    |
|---|--------------------|
| CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES | <u>\$ (11,610)</u> |
|---|--------------------|

See accompanying notes to the basic financial statements.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2006

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Tax Increment Financing Authority (TIFA) conform to generally accepted accounting principles as applicable to governments. The following is a summary of the more significant policies:

FINANCIAL REPORTING ENTITY

The Tax Increment Financing Authority (TIFA) (the "Authority") is organized and incorporated as authorized by and pursuant to the Tax Increment Finance Authority Act, P.A. 450 of 1981, as amended. The Authority is a component unit of the City of Litchfield, Michigan governed by a separate board appointed by the City Council, created to promote economic growth in the City of Litchfield, Michigan.

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all activities of the Authority. Authority's government-wide activities are considered governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenue includes (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function, and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes, intergovernmental payments, and other items not included among program revenues are reported instead as general revenue. Note: during the year, the Authority did not receive any program revenues.

MEASUREMENT FOCUS, BASIS OF ACCOUNTING, AND FINANCIAL  
STATEMENT PRESENTATION

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Property taxes, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be available only when the government receives the cash.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2006

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BUDGETS AND BUDGETARY ACCOUNTING

The Authority's procedures in establishing the budgetary data reflected in the financial statements are as follows:

1. The Authority's Board submits to the City Council a proposed operating budget for the fiscal year. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to July 1, the budget is legally enacted through passage of a resolution.
4. Formal budgetary integration is employed as a management control device during the year.
5. The budget is adopted on a basis consistent with generally accepted accounting principles, which is the modified accrual basis used to reflect actual results, and consist only of those amounts contained in the formal budget approved or as amended by City Council. The budget is adopted at the fund level.

ENCUMBRANCE ACCOUNTING

Encumbrances for goods and services are documented by requisitions or contracts. Appropriations lapse at June 30 and any encumbrances outstanding at that time are to be either canceled or appropriately provided for in the subsequent year's budget. There were no outstanding encumbrances at June 30, 2006.

PROPERTY TAX

The City of Litchfield, the primary government, bills and collects property taxes and distributes them to the Authority. Properties are assessed as of December 31, and the related real property taxes are levied and become payable on July 1 of the following year for summer taxes and December 1 for winter taxes. Summer and winter taxes are due without penalty if paid by September 14 and February 14, respectively. Delinquent taxes are turned over to the County and added to the County tax roll. The County remits all uncollected delinquent real property taxes to the City by June 30. Subsequently, the City remits to the Authority the portion of delinquent real property taxes due to it. Uncollected personal property taxes are not accrued because the date of collection is uncertain.

CAPITAL ASSETS

Capital assets, which include land and buildings, are reported in the government wide financial statements. The Authority defines capital assets as assets with an initial individual cost of more than \$2,000 and an estimated useful life in excess of 2 years. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Costs of normal repair and maintenance that do not add to the value or materially extend an assets life are not capitalized but rather expensed in the period incurred.

Buildings are depreciated using the straight-line method over a fifty year period.



CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2006

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

RISK MANAGEMENT

The Authority is exposed to various risks of loss related to property loss, torts, errors and omissions. The Authority is covered under the City of Litchfield's commercial insurance as a coinsurer for general liability for the aforementioned risks.

There have been no reported claims to the commercial insurance with respect to the Authority in any of the past three years. Additionally, there were no reductions in coverage's obtained through the City of Litchfield's commercial insurance during the past year.

NOTE 2: DEPOSITS AND INVESTMENTS

Michigan Compiled Laws, Section 129.91, authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The Authority is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and that matures not more than 270 days after the date of purchase; obligations of the State of Michigan or any of its political subdivisions that at the time of purchase are rated as investment grade by not less than one standard rating service; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The breakdown between deposits and investments for the Authority is as follows:

|  |                     |
|--|---------------------|
| Cash (checking accounts, savings accounts<br>and certificates of deposits) | \$ 1,207,755        |
| Investment in a money market fund  | <u>607,651</u>      |
| Total  | <u>\$ 1,815,406</u> |

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2006

NOTE 2: DEPOSITS AND INVESTMENTS (CONCLUDED)

Deposits

The Authority's deposits were reflected in the accounts of the bank at \$1,815,443. Of that amount, \$303,403 was covered by federal depository insurance and the remainder was uninsured and uncollateralized.

The Authority believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Authority evaluates each financial institution with which it deposits Authority funds and assesses the level of risk of each institution; only those with an acceptable estimated risk level are used as depositories.

Investments

Investments are normally categorized to give an indication of the level of risk assumed by the Authority. As of June 30, 2006, the Authority's investment in a money market fund, totaling \$607,651, was rated AAA by Standard & Poor's rating service. Additionally, there is no custodial risk because the fund is not evidenced by securities that exist in physical or book entry form. The Authority believes that its investment in the money market fund is in compliance with Public Acts 196 of 1997. The money market fund is registered with the SEC.

NOTE 3: INVESTMENT IN LAND AND INFRASTRUCTURE DEVELOPMENT

Investment in land represents land developed by the Authority for residential housing and industrial expansion. The Authority anticipates selling the land to developers. Additionally, TIFA is investing in the development of infrastructure in the new residential housing complexes. When the development is complete the infrastructure will be contributed to the City of Litchfield at which time it will be capitalized and depreciated in the financial books of the City.

NOTE 4: LONG-TERM NOTES RECEIVABLE

During the year the Authority loaned \$100,000 to Newco Industries, Inc. for improvements to the Company's newly acquired operating facility. The terms of the loan require interest only payments commencing on February 1, 2006 through January 1, 2007. Effective February 1, 2007 the Company is required to pay the Authority minimum monthly installments of \$1,700, which includes interest at the rate of 5.0% per annum, through January 31, 2010 at which time any remaining principal is due in full.

\$ 100,000

During 2004-2005 fiscal year the Authority loaned \$500,000 to Newco Industries, Inc. to acquire land and building located in City of Litchfield. The terms of the loan require the Company to repay the Authority \$400,000 in monthly installments of \$3,680, which includes interest at the rate of 2.0% per annum, effective July 22, 2005 through June 21, 2015; the remaining \$100,000 was forgiven by the Authority as a grant.

374,592

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
JUNE 30, 2006

NOTE 4: LONG-TERM NOTES RECEIVABLE (CONCLUDED)

During the year the Authority loaned \$102,389 to Payseno Builders, a construction contractor, for cost incurred in the construction of condominiums in City of Litchfield. The terms of the loan require the contractor to repay the Authority \$5,000 on the sale of each condominium until the full amount borrowed is repaid, interest free. Since the condominiums will be sold on unknown dates imputed interest is indeterminable.

\$ 102,389

\$ 576,981

Less: current portion of notes receivable

54,798

TOTAL LONG-TERM NOTES RECEIVABLE

\$ 522,183

|               | <u>7/01/05</u>    | <u>Additions</u>  | <u>Reductions</u> | <u>6/30/06</u>    |
|---------------|-------------------|-------------------|-------------------|-------------------|
| Newco 1/31/10 | \$                | \$ 100,000        | \$                | \$ 100,000        |
| Newco 6/21/15 | 500,000           |                   | 125,408           | 374,592           |
| Payseno       |                   | 102,389           |                   | 102,389           |
|               | <u>\$ 500,000</u> | <u>\$ 202,389</u> | <u>\$ 125,408</u> | <u>\$ 576,981</u> |

Following is the maturity schedule of outstanding notes receivable:

| <u>June 30</u> | <u>Principal</u>  | <u>Interest</u>  | <u>Total</u>      |
|----------------|-------------------|------------------|-------------------|
| 2007           | \$ 54,798         | \$ 12,809        | \$ 67,607         |
| 2008           | 54,078            | 10,488           | 64,566            |
| 2009           | 55,667            | 8,899            | 64,566            |
| 2010           | 100,066           | 7,252            | 107,318           |
| 2011           | 40,335            | 3,831            | 44,166            |
| 2012-2015      | 169,648           | 7,017            | 176,665           |
| Thereafter     | 102,389           |                  | 102,389           |
|                | <u>\$ 576,981</u> | <u>\$ 50,296</u> | <u>\$ 627,277</u> |

The Payseno Builders note is reported as thereafter since the date of collection is indeterminable.

CITY OF LITCHFIELD, MICHIGAN  
TAX INCREMENT FINANCING AUTHORITY (TIFA)  
NOTES TO FINANCIAL STATEMENTS (CONCLUDED)  
JUNE 30, 2006

NOTE 5: CHANGES IN FIXED ASSETS

A summary of capital assets of the Authority activities was as follows:

|                                   | <u>Balance<br/>7/01/05</u> | <u>Additions</u>  | <u>Disposals &amp;<br/>Adjustments</u> | <u>Balance<br/>6/30/06</u> |
|-----------------------------------|----------------------------|-------------------|--|----------------------------|
| Assets not being depreciated:     |                            |                   |  |                            |
| Land                              | \$ 35,000                  | \$                | \$                                     | \$ 35,000                  |
| Capital assets being depreciated: |                            |                   |  |                            |
| Building                          | <u>315,000</u>             | <u>          </u> | <u>          </u>                      | <u>315,000</u>             |
|                                   | <u>\$ 350,000</u>          | <u>\$</u>         | <u>\$</u>                              | <u>\$ 350,000</u>          |
| Accumulated depreciation:         |                            |                   |  |                            |
| Building                          | <u>\$ 44,100</u>           | <u>\$ 6,300</u>   | <u>\$</u>                              | <u>\$ 50,400</u>           |
| Net Capital Assets                | <u>\$ 305,900</u>          | <u>\$ 6,300</u>   | <u>\$</u>                              | <u>\$ 299,600</u>          |

NOTE 6: LEASES

The Authority leases property to a local manufacturer for \$2,750 per month renewable annually. At year ended June 30, 2006, the Authority recognized lease revenue in the amount of \$33,000.

NOTE 7: PROPERTY TAX ADJUSTMENTS

During the year TIFA repaid taxes collected totaling \$32,573 resulting from Board of Review decisions in favor of taxpayer claims.

Additionally, the State of Michigan determined that TIFA captured school tax dollars one year too many in accordance with the Tax Increment Finance Act. As a result TIFA is required to remit \$150,000 it captured during the 2004 tax year back to the schools. At June 30, 2006 TIFA accrued the obligation as a liability under due to other governmental units.

Both of the above are recorded as other expenditures.

## OTHER REPORTS



Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

184 West Carleton Road

Hillsdale, Michigan 49242

Telephone: 517/439-9331

FAX: 517/439-1894

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND OTHER  
MATTERS AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED  
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Tax Increment Financing Authority Board  
City of Litchfield, Michigan  
Litchfield, Michigan

We have audited the financial statements of the governmental activity and fund information of the Tax Increment Financing Authority (TIFA), a component unit of City of Litchfield, Michigan, as of and for the year ended June 30, 2006, which collectively comprise the Tax Increment Financing Authority (TIFA), Michigan's basic financial statements and have issued our report thereon dated October 5, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Tax Increment Financing Authority (TIFA), a component unit of City of Litchfield, Michigan, financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Tax Increment Financing Authority (TIFA), a component unit of City of Litchfield, Michigan, internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of the Tax Increment Financing Authority (TIFA) Board, City Council, management, and the State of Michigan. However, this report is a matter of public record and its distribution is not limited.

*Osbourne, March, Condon & Co P.C.*

Certified Public Accountants

Hillsdale, Michigan  
October 5, 2006